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THE UKRAINIAN WAR ECONOMY

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Ukraine has been subject to full-scale Russian aggression since 24 February 2022, with major implications for Ukraine's economic performance and economic management. Martial law has temporarily restricted civil and political rights and allowed the government to introduce command management in the economic sphere. These war-related prerogatives have been used only partly (for example, in the energy and transportation sectors, restricting convertibility of the hryvnia and banking transactions with foreign currency), while the dominant role of the private sector and market forces has been maintained in other respects.

As a result of war damages and territorial losses, Ukraine's real GDP contracted by about 30 percent in 2022. Ukraine also experienced severe balance-of-payments and budget tensions in the first months of the war. Intensification of foreign financial aid from the second half of 2022 helped to achieve relative macroeconomic stability in the first half of 2023. The prospects of the Ukrainian economy depend on the length of the war, associated damages and the size of external financial aid.

Before February 2022, Ukraine's record of economic and governance reform was mixed; the war stopped most reforms. On the other hand, obtaining European Union candidate status in June 2022 provided a new incentive to implement comprehensive governance reforms related, in particular, to the judicial system, media, national minorities, public transparency and fighting corruption.

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1 Introduction

Ukraine has been subject to full-scale Russian aggression since 24 February 2022[1]. Understandably, the focus of international public opinion and the expert community has been the military and political developments in Ukraine and around, international sanctions against the aggressor, aid to Ukraine, and prospects for post-war reconstruction (see, for example Gorodnichenko *et al*, 2022; Boyarchuk *et al*, 2023; Aslund and Kubilius, 2023). Less attention is given to how the Ukrainian economy has been managed during the war and how it has performed[2]. The question of economic management will become increasingly critical as the conflict continues.

This paper analyses Ukraine's war economy management and performance, according to information available in June 2023. We begin with a brief description of the Ukrainian economy at the end of 2021, that is, after the termination of most of the COVID-19-related administrative restrictions and in the middle of Volodymyr Zelensky's presidential term, but before the beginning of the Russian aggression (section 2). Section 3 describes the mechanism of war economy management. Section 4 analyses macroeconomic management in war conditions. Section 5 discusses economic performance in 2022 and 2023. Section 6 looks at the progress of Ukraine's integration into the European Union since the European Council decision of 23 June 2023 to grant Ukraine and Moldova EU candidate status (see European Council, 2022). Section 7 contains policy conclusions and recommendations.

Our analysis is based on International Monetary Fund, World Bank and UN agency databases, Ukraine's official data sources and the estimates of Ukrainian and international experts and think tanks. However, part of the 2022 data used in our analysis still has a preliminary character. In particular, this concerns GDP estimation. It does not include the occupied territories.

2 The Ukrainian economy before the war (2020-2021)

Like other countries, Ukraine was heavily hit by the COVID-19 pandemic in 2020-2021, which continued in 2022-2023 after the war began. By 10 June 2023, the recorded number of infections amounted to 5,556,030. By the same date, the pandemic was responsible for 112,394 death cases, approximately 0.26 percent of the total population[3].

Although the GDP decline in 2020 was modest (by 3.8 percent) compared to other European or Latin American economies, it came on top of disappointing growth records in the previous 30 years (Dabrowski, 2023). In 2021, GDP recovered to the pre-pandemic level.

However, in 2019, Ukraine's income *per capita* level in purchasing power parity terms in international dollars was approximately the same as in 1992 and lower than in 2008 (Figure 1). It is the worst growth performance among the post-communist countries in Central and Eastern Europe and the former Soviet Union.

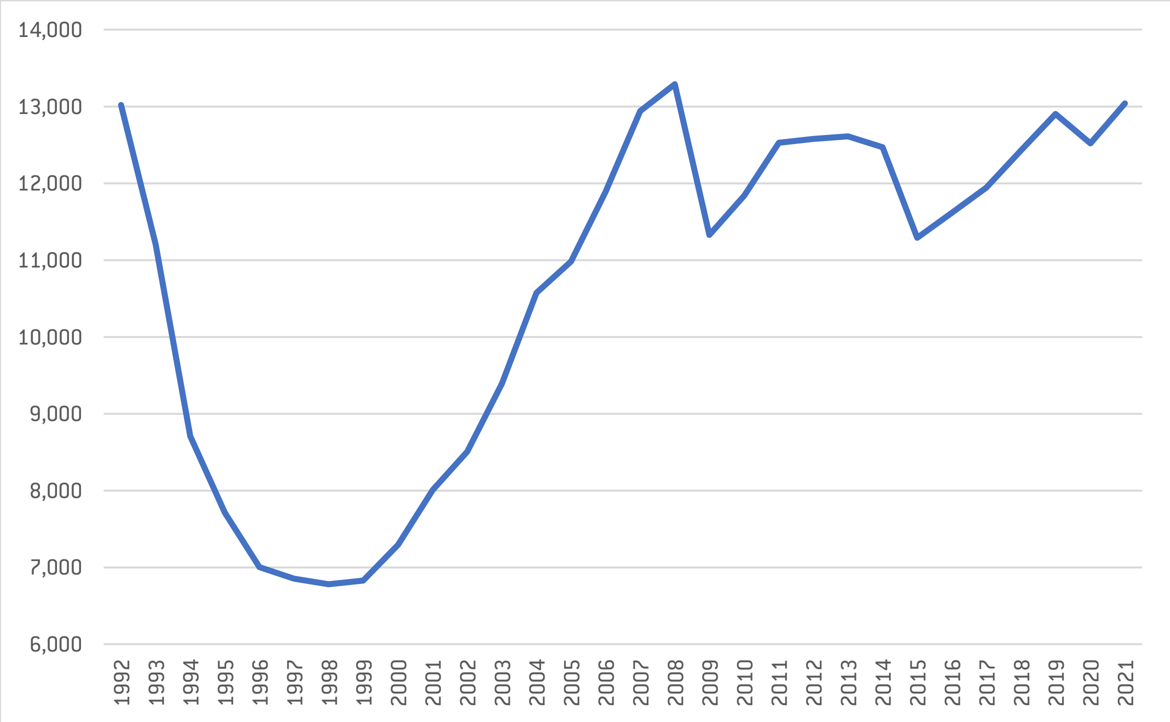
There are several reasons for this gloomy picture: structural and institutional distortions inherited from the Soviet era, the late start of macroeconomic stabilisation and liberalisation (end of 1994) and slow and chaotic reforms in the 1990s and 2000s, which led to macroeconomic and financial crises in 1993, 1998-1999, 2008-2009 and 2014-2015 (Dabrowski, 2007; 2017). The first round of Russian aggression in 2014-2015 (annexation of Crimea and war in Donbas) and other unfriendly moves (for

[1] Previously, in 2014 Russia annexed Crimea and initiated a proxy war in Donbas, which continued at low intensity until February 2022.
[2] Monthly reports, webinars and frequent online updates of the Kyiv-based Centre for Economic Strategy (see http://ces.org.ua) are notable exceptions.
[3] See https://www.worldometers.info/coronavirus/#countries.

example, revoking a Russia-Ukraine free trade agreement on 1 January 2016) were severe blows to the Ukrainian economy and increased the security risk for investment and business activity.

The slow pace of reforms helped build powerful oligarchic groups[4] that benefitted from macroeconomic imbalances, structural distortions and opaque legislation. They parasitised on numerous state-owned enterprises (SOEs) and captured national and local politics.

Figure 1: GDP *per capita*, constant prices, purchasing power parity, 2017 international dollar, 1992-2021



Source: IMF World Economic Outlook database, October 2022.

Since 2014, reforms in Ukraine have accelerated and become more comprehensive in the wake of the Revolution of Dignity (Dabrowski *et al*, 2020). Nevertheless, several important policy areas and institutions have remained unreformed or partially reformed. Among others, this is the case for the judicial system (and, more generally, the rule of law), law enforcement and security agencies, public administration, media, local and regional self-government, tax and customs administration, and a large sector of SOEs and state-owned banks, which should be privatised (Boyarchuk *et al*, 2023). The discharge of the relatively technocratic, reform-minded government led by Oleksiy Honcharuk in March 2020 slowed the pace of reforms. It caused a partial reversal of the previous reform achievements (Prokopenko, 2021).

[4] See Goriunov *et al* (2023) for a comprehensive analysis of oligarchic groups in Ukraine.

3 The war economy management (2022-2023)

The Russian aggression, which started on 24 February 2022, triggered the immediate introduction of martial law by Presidential Decree No. 64/2022 for 30 days, then extended several times by the Verkhovna Rada (the Ukrainian parliament)[5].

Martial law changed how the country was managed in many essential areas. Civil and political rights were temporarily restricted, some opposition political parties considered pro-Russian were suspended, all national television channels were consolidated into one platform, and military censorship was introduced. The general mobilisation was announced and men aged 18-60 were banned from leaving the country without special permission. Central authorities could impose curfews, restrict movement within the country, search homes and property, control correspondence and take over private and communal property for state needs.

The establishment of martial law had repercussions on territorial administration. Territorial communities played a critical role over the first days and even weeks of the war when the operability of the central power was seriously damaged. The leaders of local communities predominantly stayed in place and started acting independently according to their situation. In this context, martial law established local military administrations subordinated to the President, which operated alongside civilian administrations and leaders in all territorial units (oblast [region], rayon [district], municipality). In May 2022, the prerogatives of local military-civilian administrations were expanded to improve the system's manageability. Although the President can appoint and dismiss heads of local military administrations, in most cases, elected leaders of local communities have been nominated for these positions.

Economic-policy priorities and management mechanisms had to be subordinated to war needs, the need to defend the country, save the population, supply the army and scale up military production. Among other prerogatives, military administrations acquired the right to use capacities and labour resources of enterprises, institutions and organisations of all forms of ownership for defence needs. The logic of the war economy led to command management and administrative restrictions in many policy areas. On the other hand, some extraordinary circumstances forced authorities to permit more flexibility and economic freedom, at least temporarily.

Before the war, the government performed some price monitoring for socially essential commodities, including some fuels. Since the start of the war, the authorities did not introduce any additional price regulations. On the contrary, after missile attacks on Ukraine's main refinery and fuel deposits triggered a fuel crisis in May-July 2022, the authorities eased price controls to incentivise traders to increase fuel imports.

However, on 24 February 2022, the National Bank of Ukraine (NBU) introduced several restrictions on foreign-exchange (FX) operations. It banned foreign cash withdrawals by individuals from accounts held in Ukrainian banks, foreign currency sale to banks, online purchases of foreign currency, loan repayments and interest payments abroad. Legal entities were allowed to spend foreign currency for critical imports, according to the list defined by the authorities. Upper limits were introduced for cashless operations from hryvnia (UAH) credit and debit cards abroad. That is, both the capital account

[5] At the end of 2018, then President Petro Poroshenko introduced martial law for 30 days in ten regions of East and South Ukraine as the reaction to the blockade of the Kerch Strait by Russia.

and current convertibility of the Ukrainian currency were effectively suspended[6]. Since then, some of these measures have been eased or adapted to new circumstances (see subsection 4.1).

Simultaneously with convertibility restrictions, the NBU fixed the official exchange rate at UAH 29.25 for $1.

The Cabinet of Ministers allowed procuring agencies to purchase everything necessary for the war through direct contracts out of the scope of the Prozorro electronic procurement system. However, in June 2022, the Cabinet resumed public procurement via Prozorro, with many exceptions related to urgent military needs. Changes in government procurement have been frequent and significant, with additional modifications occurring at the end of 2022 and the beginning of 2023. In the first quarter of 2023, efforts were made to reintroduce competitive bidding while adapting to the evolving situation. These were speeded up by, among other instances, a series of procurement scandals at the Ministry of Defence revealed in January and February 2023[7].

The anti-corruption measures, which frequently suffered from political infighting and pressures of various lobbies in 2019-2021 (Boyarchuk and Dabrowski, 2020), were intensified when the war started. The primary political motivation was the need for external funding, conditional on the progress in fighting corruption. This led to the appointment of a truly independent new Specialised Anti-Corruption Prosecutor (SACP) in July 2022, which had been resisted earlier. This move unlocked dozens of high-ranking corruption cases passed to the court by the SACP.

The term of the first Head of the National Anti-Corruption Bureau (NABU), Artem Sytnyk, expired in April 2022. The authorities initiated a competitive selection process, and by March 2023, Semen Kryvonis was appointed as the new Head of NABU.

NABU investigated several high-profile corruption cases, including cases involving leading officials in the Supreme Court and State Property Fund[8]. However, some decisions taken by anti-corruption bodies have raised doubts about whether they are politically motivated, particularly in the cases of prosecutions of Andriy Kobolev, the former Head of Naftogaz, and Andriy Pyvovarskiy, the former Minister of Infrastructure[9].

In November 2022, under martial law, the government took over temporarily the private shares of five companies: the gasoline chain Ukrnafta, petroleum refiner Ukrtatnafta, MotorSich, heavy-duty truck maker AvtoKrAZ, and power transformer manufacturer Zaporizhtransformator. These shares will be returned to the original owners when the war ends. These five companies produce commodities critical to the war effort but some owners have been suspected of links to the Kremlin. In particular, Vyacheslav Bohuslayev, the owner of MotorSich, which makes aircraft and helicopter engines, was accused of treason and arrested. Despite a ban on such sales, Bohuslayev supplied helicopter engines

[6] Before the war, Ukraine had several restrictions on capital account transactions, and a few on current account transactions (see IMF, 2022).
[7] Adrian Karatnycky, 'Corruption, fraud and Ukraine's defense minister', *Politico*, 11 February 2023, https://www.politico.eu/article/ukraine-war-corruption-fraud-defense-minister-oleksii-reznikov/.
[8] Liza Brovko, 'Knyazev' s case: NABU searched three judges of the Supreme Court', *Babel*, 13 June 2023, https://babel.ua/en/news/95051-knyazev-s-case-nabu-searched-three-judges-of-the-supreme-court; Andrii Marusov, 'Why Sennychenko's High-Profile Corruption Case is a Potential Time Bomb', *Kyiv Post*, 17 April 2023, https://www.kyivpost.com/post/15936.
[9] Aleksandra Klitina, 'The Cases Against Kobolev and Pyvovarsky Are a Mistake – Head of NABU's Supervisory Council', *Kyiv Post*, 6 March 2023, https://www.kyivpost.com/post/13886; Patrick Wintour, 'High stakes for Ukraine as clampdown on corruption comes under scrutiny', *The Guardian*, 18 April 2023, https://www.theguardian.com/world/2023/apr/18/high-stakes-for-ukraine-as-clampdown-on-corruption-comes-under-scrutiny.

to Russia[10]. Although the government take over of these assets has clear security logic, it has triggered considerable concern about how this move might affect Ukraine's post-war investment prospects.

The privatisation process, which was slow before the war, was frozen when the war started. However, in July 2022, privatisation procedures were simplified, and sales of small objects of state property resumed. In 2022, revenues from privatisation were only UAH 1.7 billion (or nearly $53 million).

4 Macroeconomic management

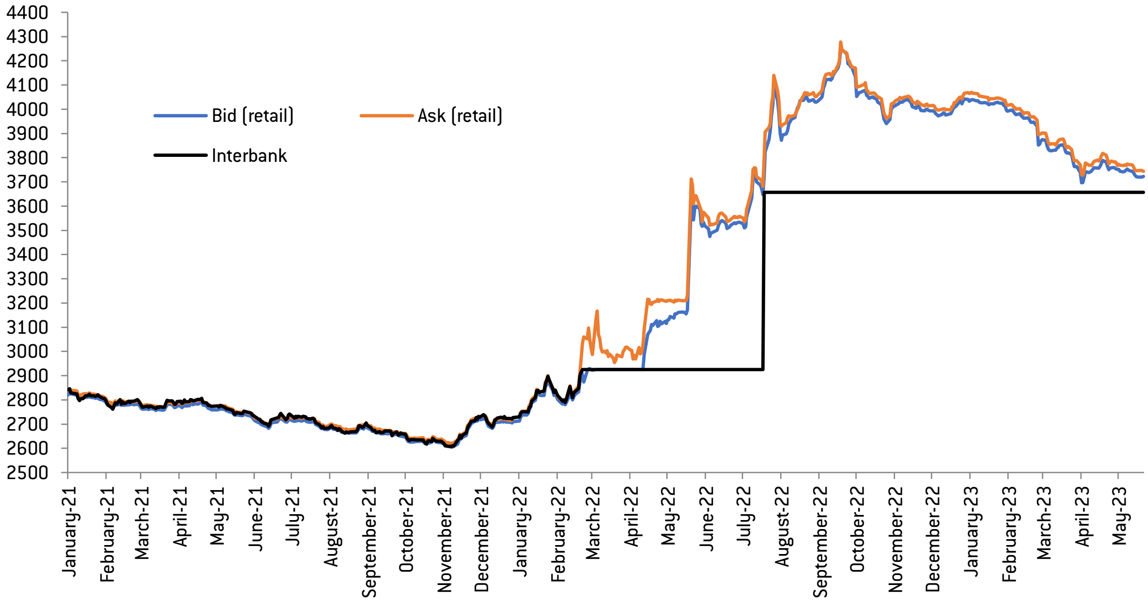
The shock generated by the Russian aggression required a macroeconomic policy response on several fronts to stabilise the balance of payments, FX market, banking sector, domestic prices, budget, etc. In the first months of the war, the NBU and government had to rely mainly on their resources and policy measures. Since the second half of 2022, the increasing foreign aid flows helped stabilise monetary and fiscal accounts and, therefore, the balance of payments and exchange rate. Below we analyse each of the critical macroeconomic policy areas.

4.1 Balance of payments, forex regulations, exchange rate

The NBU decisions on limiting UAH convertibility and fixing the exchange rate (see section 3) stabilised the situation on the FX market in the first days of the Russian invasion.

However, the necessity to finance the rapidly increasing budget deficit (as a result of additional, war-related expenditure and shrinking revenue – see subsection 4.3) through NBU credit generated substantial pressure on the FX market, forcing the NBU to increase FX interventions up to $4 billion per month by June 2022. Eventually, the NBU devalued the official exchange rate to UAH 36.57 per $1 in July 2022.

Figure 2: Exchange rate dynamics (UAH per $100), January 2021-March 2023



Source: National Bank of Ukraine.

[10] Kira Tolstyakova and Kyrylo Ovsyaniy, 'Detained Ukrainian Industrialist, Suspected of Collaboration, Requests Transfer To Russia', *Radio Free Europe/ Radio Liberty*, 13 May 2023, https://www.rferl.org/a/ukraine-schemes-bohuslayev-russia-exchange/32410114.html.

The devaluation of the official exchange rate eased market pressure for a while, but the FX market remained volatile amid continued deficit financing and volatility of foreign financial aid. The difference between retail and official exchange rates exceeded 10-15 percent (Figure 2). The tension eased after the NBU allowed purchases by individuals for saving reasons (ie with the immediate deposit of the purchased foreign currency into a savings account in the Ukrainian bank) of foreign cash at a rate close to the official rate. The difference between official and retail rates remained high, but started narrowing gradually.

The increase in reserve requirements for commercial banks in January 2023, with subsequent reduction of excessive liquidity in the banking system, strengthened UAH against the dollar on the retail market, reducing the gap between the retail and official exchange rates in early April 2023. The future situation in the FX market will depend on the size of foreign financial aid.

Export and import operations in the first weeks of the war almost stopped. In March 2022, exports of goods plummeted by 51.6 percent y/y and imports by 64.7 percent y/y[11]. Exports of services also dropped by 21.7 percent y/y (due to falling transportation services) while imports of services surged by 85.2 percent y/y due to spending of Ukrainian refugees abroad. In May 2022, when it became clear that the Russian assault had failed, imports started reviving fast, while all other trends remained unchanged.

In 2022 exports of goods fell by 35.2 percent y/y, and imports of goods fell by 19.4 percent y/y. Exports of services dropped by 12.4 percent y/y, and imports of services surged by 85.7 percent y/y. The trade deficit on goods ballooned to $15.3 billion (from $6.6 billion in 2021). Balance on services switched into the red with a $10.7 billion deficit in 2022 vs a $4.0 billion surplus in 2021.

Despite a large trade deficit, the current account balance recorded a $8.0 billion surplus in 2022 vs a $3.9 billion deficit a year earlier. The surge in foreign grants from $4.6 billion in 2021 to $25.3 billion in 2022, and a sharp decrease in interest payments ($4.4 billion vs $19.4 billion a year earlier), because of the martial-law regulations (see above), were responsible for this improvement. Additionally, incoming remittances of Ukrainian labour migrants remained high despite the war and amounted to $13.1 billion in 2022, compared to $13.6 billion in 2021.

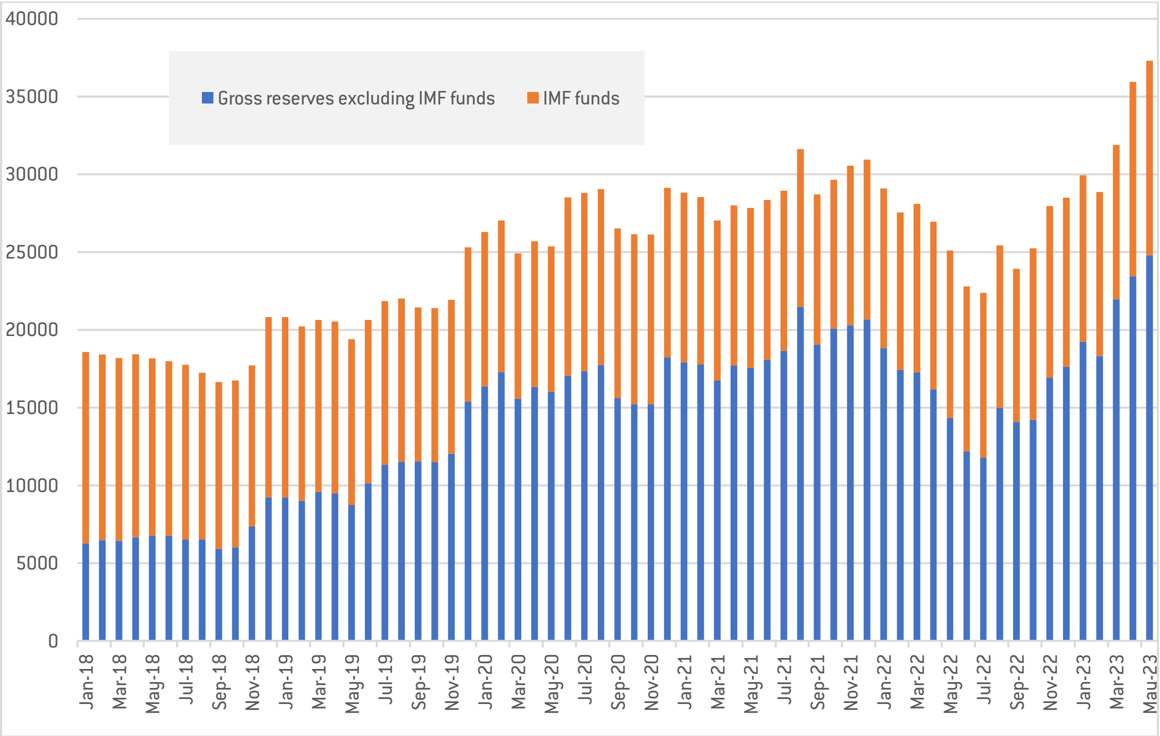
Financial and capital account balance deteriorated in 2022, recording a net outflow of $10.9 billion compared to $4.4 billion in net inflow in 2021. Foreign cash withdrawal from the banking system ($10.3 billion) and trade credits ($12.6 billion) were the main channels of foreign currency outflow. Extensive official external borrowing of $14.8 billion could not compensate for it.

Gross international reserves remained strong thanks to foreign loans and grants (Figure 3). By the end of February 2022, they amounted to $27.6 billion. They were reduced to $22.4 billion at the end of July 2022. However, at the end of 2022, they exceeded the pre-war level, reaching $28.5 billion. By the end of May 2023, they amounted to $37.3 billion. Remarkably, during the first 12 months after the start of the war, the NBU spent on FX interventions $28.8 billion (Figure 4), that is, more than what the gross reserves amounted to when the war began.

Foreign financial aid is the primary resource, stabilising Ukraine's balance of payments, NBU gross international reserves, the UAH exchange rate, domestic price levels and the state budget, and providing sufficient liquidity to the banking sector (see subsection 4.4).

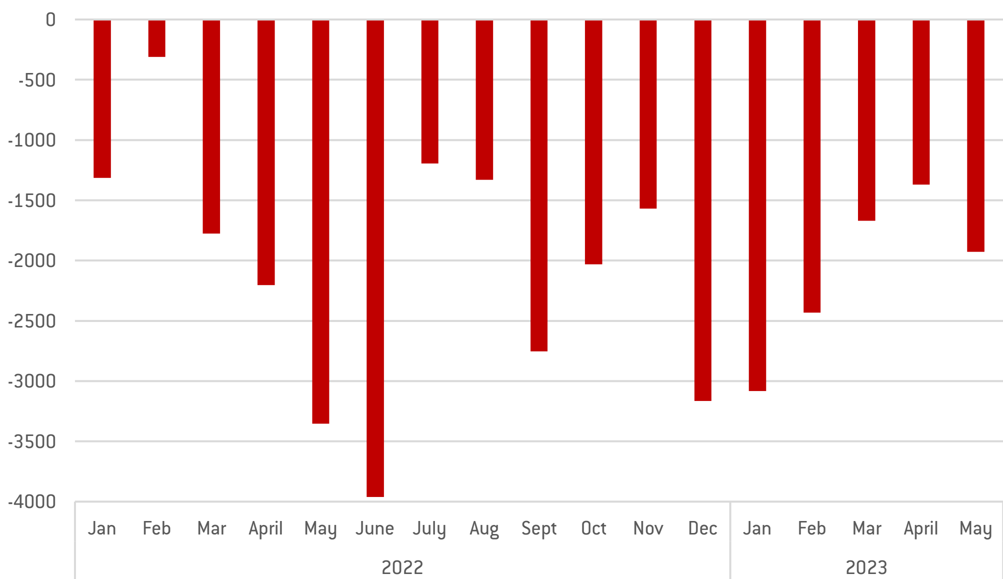
[11] Data on exports, imports, trade balance, capital account balance, exchange rate and gross international reserves used in this subsection come from the NBU statistics.

Figure 3: NBU Gross International Reserves, $ billions, January 2018-May 2023



Source: IMF, National Bank of Ukraine.

Figure 4: The NBU net FX interventions, $ millions, January 2022-May 2023

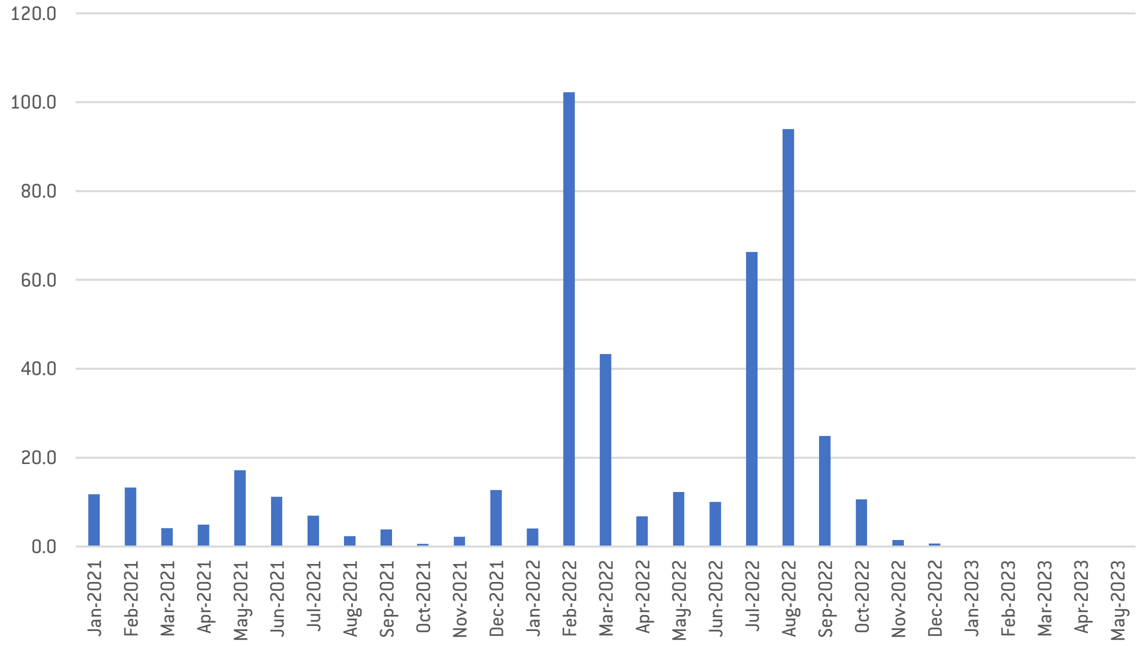


Source: National Bank of Ukraine.

4.2 Monetary management

Since the beginning of the full-scale Russian invasion, the NBU has focused on maintaining the functionality of the banking system and supporting monetary stability. It provided banks with ample refinancing options to ensure the safety and liquidity of the banking system (Figure 5). In just the last three days of February 2022 banks received UAH 92.3 billion via the refinancing channel (equivalent to $3.2 billion). Then the size of this support went down, amounting to UAH 43.3 billion ($1.5 billion) in March 2022. The second wave of support came in July and August 2022. Then it went rapidly down, practically disappearing in the first five months of 2023. This was the effect of the high level of liquidity in the banking sector.

Figure 5: NBU refinancing of the banking sector, billions UAH, January 2021 – February 2023



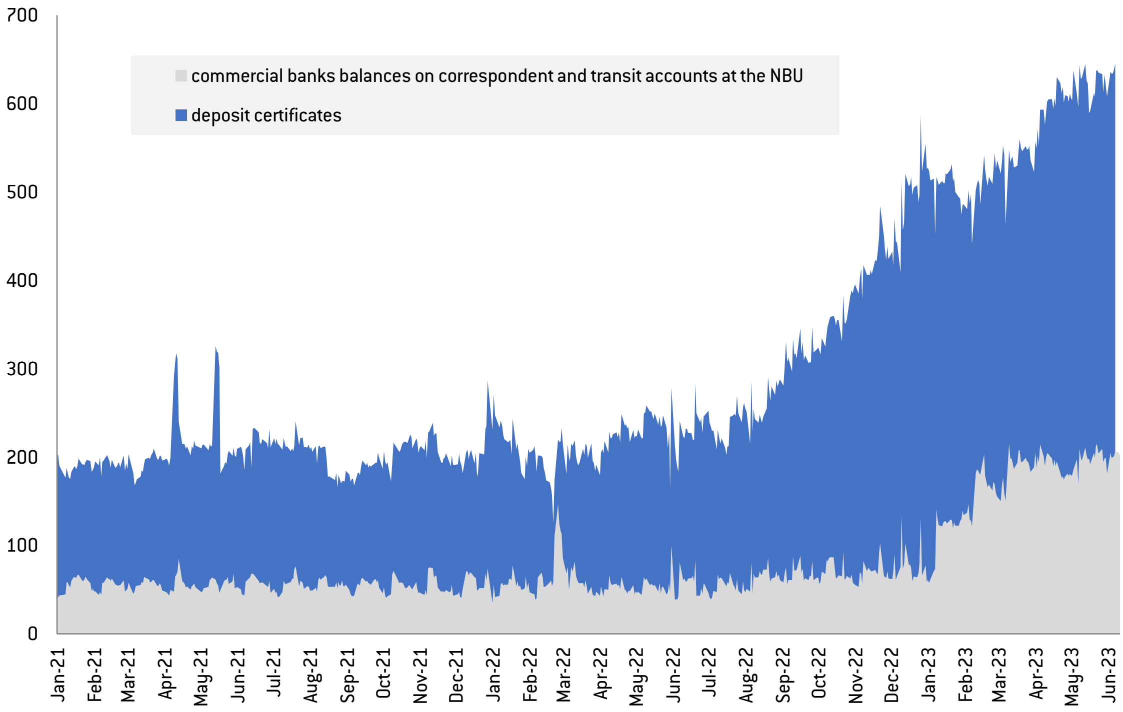
Source: National Bank of Ukraine.

The residual balances in commercial banks' correspondent and transitory accounts at the NBU amounted to above UAH 120 billion ($4.1 billion) per day towards the end of February 2022 and the beginning of March 2022. This was well above the pre-war level of UAH 50 billion to 60 billion ($1.7 billion to $2.1 billion) daily (Figure 6).

In March 2022, the liquidity was additionally maintained by an increase in the NBU portfolio of Treasury bonds (T-bonds) by UAH 20 billion ($0.7 billion). By the end of 2022, the value of T-bonds held by the NBU had increased by UAH 394.4 billion ($12.2 billion) (Figure 7). On the other hand, NBU interventions in the FX market and the emission of the NBU deposit certificates (see subsection 4.1) reduced UAH liquidity.

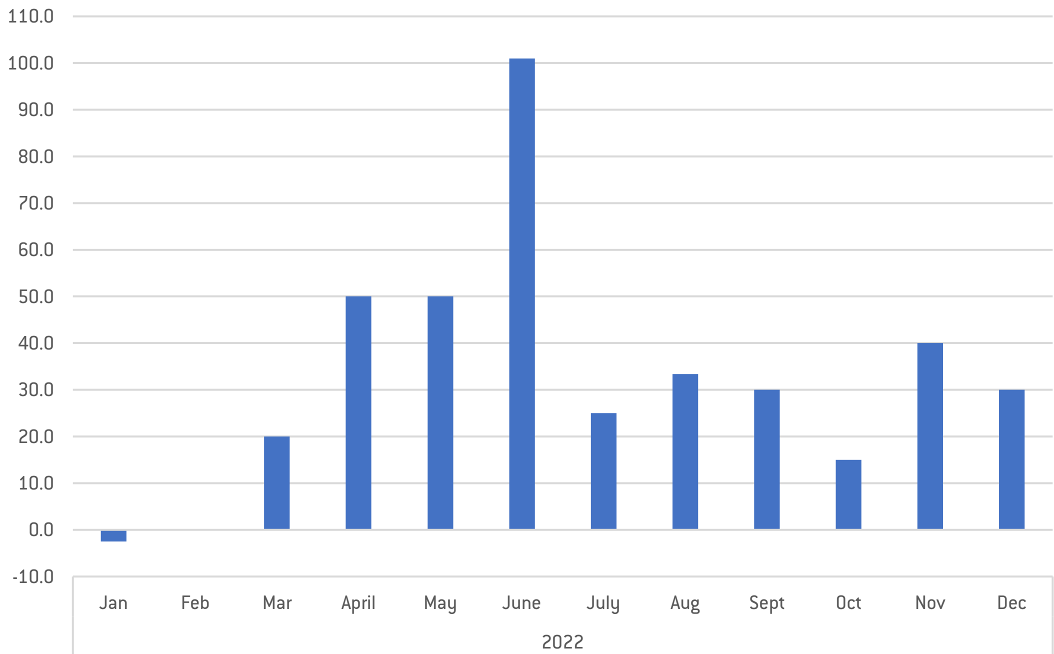
Initially, on 4 March 2022, the NBU left the prime interest rate unchanged at 10 percent because of the prevailing uncertainty (Figure 8). However, excessive pressure on the FX market and abundant liquidity forced the NBU to raise the prime rate by 15 bps to 25 percent starting 3 June 2022. The refinancing rate was 27 percent, while the overnight deposit certificate rate was 23 percent.

Figure 6: Liquidity of the banking system, UAH billions, January 2021- June 2023



Source: National Bank of Ukraine.

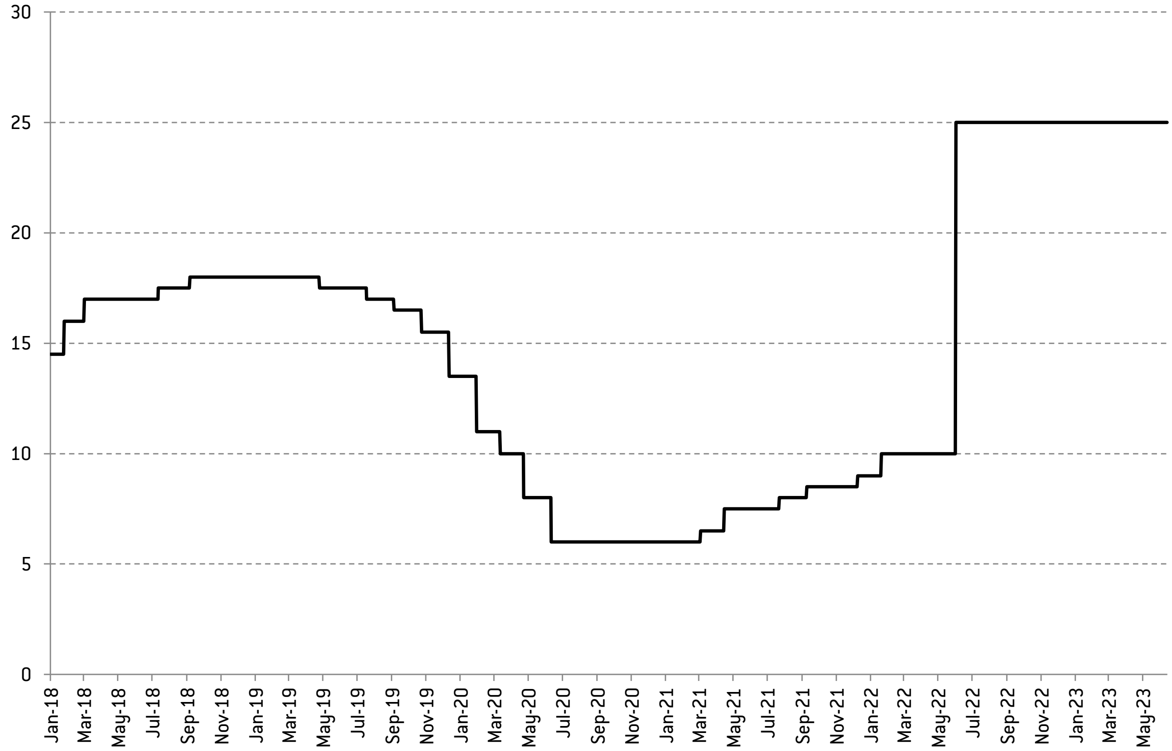
Figure 7: The NBU portfolio of T-bonds, change from the previous month, UAH billion, January – December 2022



Source: National Bank of Ukraine.

The NBU expected the Ministry of Finance would increase T-bill yields to channel the excessive liquidity towards deficit financing, thereby reducing the need for NBU credit to the government. However, the Ministry of Finance kept the rates on state bonds nearly unchanged, prompting the NBU to inject more fresh hryvnia into the system. Meanwhile, the banking system's excessive liquidity flowed into overnight deposit certificates. As a result, the stock of deposit certificates increased from UAH 141.3 billion ($4.8 billion) at the end of March 2022 to UAH 456.9 billion ($12.5 billion) by the end of 2022.

Figure 8: The NBU prime interest rate, in %, January 2018 - May 2023



Source: National Bank of Ukraine.

Table 1: Disaggregation of the monetary base and broad money dynamics, in % to the end of the previous year, 2021-2022

Item	2021				2022			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Monetary base	2.1	8.2	8.1	11.2	10.6	10.1	11.8	19.6
Net foreign assets	-8.7	-4.4	-7.6	12.1	-3.0	-24.7	4.4	27.6
Net domestic assets	0.8	2.9	2.1	0.5	3.8	40.6	45.5	65.5
Net claims on the government	1.0	3.1	2.3	0.6	3.8	40.6	45.5	65.5
Claims on other internal sectors	-0.2	-0.2	-0.2	-0.1	0.0	0.0	0.0	0.0
Other items net	10.0	9.7	13.6	-1.5	9.9	-5.8	-38.2	-73.5
Broad money (M2)	0.1	3.4	4.1	12.0	0.4	3.7	10.0	20.8
Net foreign assets	-1.8	0.6	-0.9	3.8	-0.6	-4.5	8.0	18.3
Net domestic assets	0.6	0.3	1.9	5.3	0.5	9.9	13.0	13.9
Net claims on the government	0.4	-1.3	-1.3	1.3	0.4	10.0	11.8	15.5
Claims on other sectors	0.1	1.6	3.2	4.0	0.2	0.0	1.2	-1.6
Other items net	1.4	2.4	3.1	2.9	0.5	-1.7	-11.0	-11.4

Source: National Bank of Ukraine.

By the end of 2022, foreign financial aid flows had become more regular and predictable, allowing the NBU to cease deficit financing from the beginning of 2023. Furthermore, a predictable schedule of foreign aid enabled the NBU to reduce excessive liquidity in the banking system. In January 2023, the NBU increased mandatory reserve requirements for commercial banks in two steps, effectively curbing excessive liquidity. Notably, the NBU envisaged that mandatory reserves should be held in T-bonds, thus stimulating demand for this instrument.

Fiscal deficit financed by the NBU credit and intensive FX interventions were the main factors determining the money supply in 2022. At the end of 2022, the monetary base increased by 19.6 percent and broad money (M2) by 20.8 percent, compared to the end of 2021. Table 1 shows that net credit to the government was the main factor contributing to the growth of the monetary base. In contrast, NBU intervention in the FX market worked in the opposite direction (via 'Other items net').

4.3 Fiscal management

The first months of the war were dramatic for public finances. Imports almost stopped (see subsection 3.1). In the first days of the war, the finance minister announced that customs collections were only 15 percent of the pre-war level. The authorities reacted to the shock with the abolition of value-added tax and import duties on almost all imports. Excise duties were abolished for fuel imports, and the VAT rate was cut to 7 percent from the previous 20 percent. A new form of simplified taxation (the sale tax rate of 2 percent) was introduced, with even large businesses eligible for the regime.

In March 2022, consolidated budget revenues (without off-budget funds) increased by 8.0 percent y/y on the back of advance tax payments of Ukrainian enterprises, which rushed to help government finances. However, this enthusiastic attitude did not last long. In April 2022, consolidated budget revenue (net of grants) plummeted by 34.6 percent y/y, in May 2022, by 15.8 percent y/y, and in June 2022, by 29.1 percent y/y. Taking into account external grants, revenue declined by 18.3 percent, 5.1 percent and 2.6 percent y/y, respectively[12].

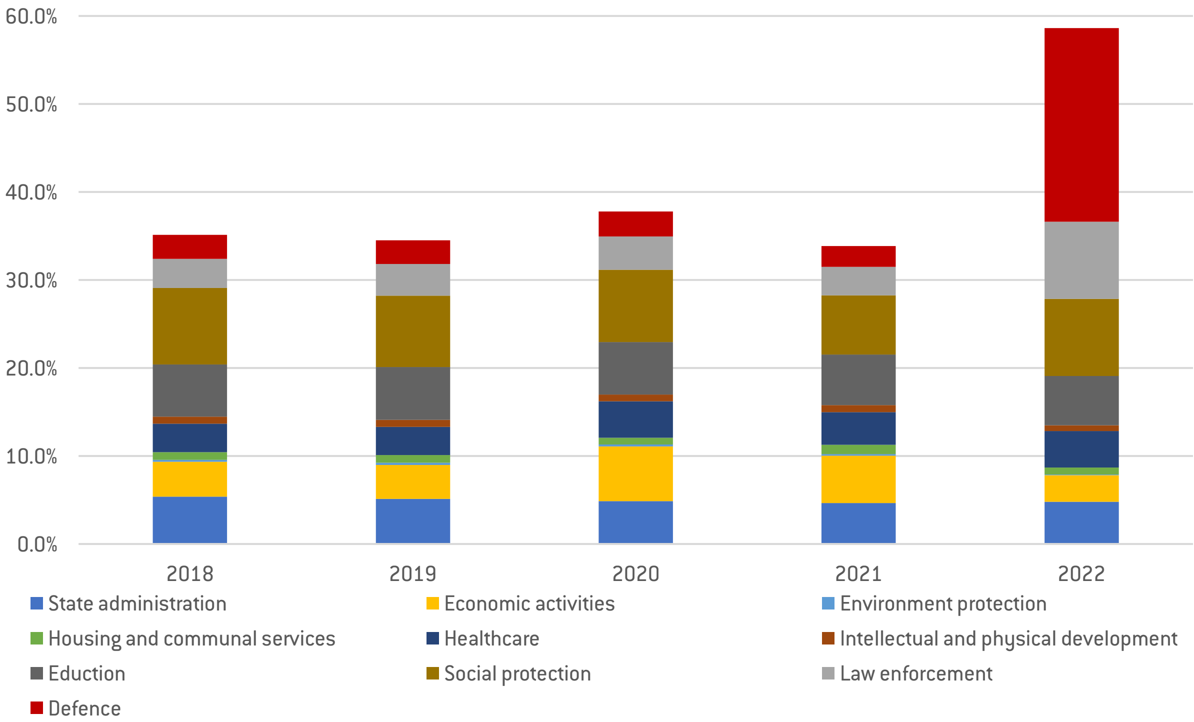
By June 2022, when the military situation stabilised, it became clear that internal economic activities would also revive after the first months of the shock. From July 2022, the authorities withdrew tax exemptions for imports and re-applied excise duties on fuel imports (although 7 percent VAT on fuels remained unchanged). Consequently, from July 2022, budget collection started improving noticeably.

A cessation of the reduced VAT rate on fuels and a limitation of the special enterprise tax regime (see above) is one of the conditions of the IMF Extended Fund Facility (EFF) programme approved in March 2023 (IMF, 2023a).

In 2022, general government (GG) revenues increased by 31.6 percent in nominal terms compared to 2021, according to the IMF World Economic Outlook database of April 2023. GG revenues increased from 36.3 percent in 2021 to 53.2 percent as a share of GDP. Such an increase can be explained by a higher nominator (nominal revenue) and a lower denominator (decline in nominal GDP). Foreign grants contributed 9.8 percent to GDP (IMF, 2023a), that is, to 18.4 percent of GG revenue. Payroll tax (social security contribution) collections grew by 21.8 percent y/y despite millions of refugees abroad and a substantial wage drop. Remuneration for the military was the primary source of payroll tax growth.

[12] Monthly fiscal data presented in this subsection come from Ministry of Finance statistics.

Figure 9: Consolidated budget expenditure (excl. pension fund): functional disaggregation, % of GDP, 2011-2022



Source: Finance Ministry of Ukraine, NBU.

Nominal GG expenditure in 2022 increased by 55.9 percent compared to 2021 and reached 69.9 percent of GDP (40.3 percent in 2021; see Table 2). Such a significant change (by almost 30 percentage points of GDP) can be explained by: (i) a considerable increase in military and security spending[13] (higher nominator), and (ii) a decline in GDP (lower denominator). Figure 9 shows a change in the functional structure of budget expenditure in 2022. Spending other than for defence, law enforcement, social protection, and healthcare was reduced substantially.

Table 2: Ukraine: principal macroeconomic indicators, 2018-2023

Item	2018	2019	2020	2021	2022	2023
Gross domestic product, constant prices, % change	3.5	3.2	-3.8	3.4	-30.3	-3.0
Inflation, e-o-p consumer prices, % change	9.8	4.1	5.0	10.0	26.6	20.0
The unemployment rate, % of the total labour force	9.0	8.5	9.2	9.8	24.5	20.9
Population, million	42.0	41.7	41.4	41.0	34.8	32.0
GG revenue, % of GDP	39.8	39.4	39.7	36.3	53.2	47.3
GG total expenditure, % of GDP	41.9	41.5	45.6	40.3	69.9	67.7
GG net lending/borrowing, % of GDP	-2.1	-2.1	-5.9	-4.0	-16.7	-20.4
GG gross debt, % of GDP	60.4	50.5	60.5	48.8	81.7	98.3
Current account balance, % of GDP	-3.3	-2.7	3.3	-1.6	5.7	-4.4

Source: IMF World Economic Outlook database, April 2023.

[13] Data on military spending does not include military aid in ammunition and equipment provided in kind by international partners.

In 2022, the GG deficit amounted to 16.7 percent of GDP (Table 2), of which 11.4 percent was financed from external sources and 7.8 percent by the NBU[14] (IMF, 2023a, Table 2, p. 62). Without 10 percent of GDP in external grants, the GG deficit would amount to 26.7 percent of GDP.

GG gross debt accounted for 81.7 percent of GDP in 2022 (Table 2), one of the highest levels recorded in the history of Ukraine. Before, the highest levels were recorded in 2015 and 2016 (79.3 percent and 79.5 percent of GDP, respectively).

After the war started, Ukraine stopped servicing the public debt to private non-residents. After approval of the IMF EFF (IMF, 2023a), Ukraine allowed repatriation of interest payments on public debt instruments received after 1 April 2023.

4.4 Foreign aid

Since the beginning of the Russian aggression, Ukraine has received large-scale foreign aid, which can be split into three broad categories: (i) military aid; (ii) humanitarian aid; and (iii) financial aid (Trebesch *et al*, 2023).

Table 3: Total aid commitments to Ukraine, by a group of donor countries and institutions, and aid category, in € billions, 24 January 2022 to 24 February 2023

Country/group of countries	Financial commitments	Humanitarian commitments	Military commitments	Total commitments
EU members and institutions	35.58	6.51	19.62	61.72
of which: EU members	*5.26*	*4.90*	*16.02*	*26.18*
EU institutions	*30.32*	*1.61*	*3.60*	*35.53*
United States	24.46	3.63	43.19	71.28
United Kingdom	2.94	0.25	6.50	9.70
Canada	1.75	0.35	1.38	3.48
Other donor countries	6.68	1.35	1.79	9.82
Non-bilateral donors	12.93	0.00	0.00	12.93
Of which: IMF	*3.19*	*0.00*	*0.00*	*3.19*
EBRD	*2.78*	*0.00*	*0.00*	*2.78*
United Nations	*0.05*	*0.00*	*0.00*	*0.05*
World Bank Group	*6.91*	*0.00*	*0.00*	*6.91*
TOTAL	**84.34**	**12.09**	**72.48**	**168.93**

Source: Kiel Institute for the World Economy, https://www.ifw-kiel.de/fileadmin/Dateiverwaltung/Subject_Dossiers_Topics/Ukraine/Ukraine_Support_Tracker/Ukraine_Support_Tracker.xlsx.
Note: EBRD = European Bank for Reconstruction and Development.

Table 3 summarises the aid commitments of 40 donor countries and multilateral donor institutions during the first year of the war (until 24 February 2023). The United States is the largest donor, especially in the military aid category. The EU and its member states go second, playing a dominant role in financial and humanitarian aid. International financial and development institutions (the IMF, World Bank Group and the European Bank for Reconstruction and Development) are substantial financial aid providers. The United Kingdom offered meaningful military aid.

It is worth remembering that the actual aid flows may differ substantially from the aid commitments in size and timing. Usually, they come later than the formal aid commitments and sometimes in smaller

[14] The NBU took over part of the T-bonds portfolio held by commercial banks (1.6 percent of GDP).

amounts than those declared. For example, as of 15 January 2023, only 48 percent of the declared budgetary support to Ukraine had been disbursed (Trebesch *et al*, 2023).

Military aid primarily has an in-kind grant character and is not included in fiscal, trade and balance-of-payments statistics computed by the Ukrainian authorities and the IMF.

Our analysis, based on IMF and Ministry of Finance of Ukraine data (see subsection 4.3), shows that financial aid played an essential role in 2022 in supplementing GG revenue (foreign grants equal to 9.8 percent of GDP) and deficit financing (foreign loans equal to 11.4 percent of GDP). They will likely play a more significant role in closing the fiscal and balance-of-payments gap in 2023.

In March 2023, the IMF Executive Board approved a 48-month EFF of $15.6 billion with an immediate disbursement of $2.7 billion (IMF, 2023a). After the successful completion of the First Review at the end of May 2023, the next tranche of $890 million was released at the end of June 2023[15]. The IMF programme paves the way for the assistance of other multilateral and bilateral donors in 2023.

Given the prospects of the prolonged and devastating war, foreign aid of various kinds will have critical importance for the continuation of military resistance against aggression, humanitarian relief and ensuring essential macroeconomic stability (avoiding currency crisis and hyperinflation).

5 Economic performance in 2022 and prospects for 2023

5.1 Real GDP

According to the IMF *World Economic Outlook* of April 2023, the real GDP of Ukraine contracted by 30.3 percent in 2022 compared to the previous year (Table 2)[16].

The same source forecasted a further decline of real GDP by 3 percent in 2023. Even if the IMF mission revised this forecast upward to annual growth of 1 percent to 3 percent during the First Review of the EFF at the end of May 2023[17], the prospects for this year look highly uncertain. The preliminary estimate of the State Statistical Service of Ukraine shows an increase of real GDP (seasonally adjusted) in the first quarter of 2023 by 2.4 percent compared to the fourth quarter of 2022, and a decline of 10.5 percent compared to the first quarter of 2022[18].

5.2 War-related material losses

Huge war material losses are another part of the story. According to the Second Rapid Damage and Needs Assessment prepared by the World Bank Group, the Government of Ukraine, the European Commission and the United Nations for the first year of the war (up to 24 February 2023), the direct damage to buildings and infrastructure amounted to $135 billion, of which 38 percent was housing, 26 percent transport, 8 percent energy, 8 percent industry and commerce, and 6 percent agriculture. The total reconstruction and recovery needs for the next ten years are estimated at $411 billion, up to 260 percent of Ukrainian GDP in 2022 (World Bank, 2023).

[15] See IMF press release No. 23/249 of 29 June 2023, https://www.imf.org/en/News/Articles/2023/06/29/pr23249-ukraine-imf-exec-board-completes-1st-rev-eff-arrangement.
[16] More recently, the State Statistical Service of Ukraine published new estimates, which show a GDP decline by 29.1 percent in 2022.
[17] See IMF press release of 30 May 2023, https://www.imf.org/en/News/Articles/2023/05/30/pr23185-ukraine-imf-and-ukrainian-authorities-reach-staff-level-agreement-eff.
[18] See https://ukrstat.gov.ua/.

Naturally, these numbers increased in the last few months as the war continued. For example, destroying the Kakhovka Dam on the Dnipro River on 6 June 2023 caused colossal material and human losses that were difficult to assess when writing this paper[19].

5.3 Inflation

The headline inflation rate measured by the consumer price index (CPI) was 26.6 percent in December 2022 (Table 2), a jump from 10 percent recorded at the end of 2021. It was the result of the record-high fiscal deficit financed partly by the NBU credit (see subsection 4.3), generous support for banking sector liquidity by the NBU (see subsection 4.2), hryvnia depreciation (subsection 4.1) and numerous supply-side shocks caused by the war.

Increasing financial aid flows, which allowed limiting the role of NBU in budget deficit financing, stabilisation of the FX market and exchange rate, and NBU measures to curb excessive liquidity of the banking sector in the second half of 2022 and first half of 2023 (see subsections 4.1-4.2) meant gradually decreasing inflation pressures. Reaching its peak in December 2022, inflation began to decline, reaching 15.3 percent y/y in May 2023. The IMF WEO of April 2023 forecasted end-of-year inflation at 20.0 percent, but the most recent NBU forecasts are more optimistic (14.8 percent). Much will depend on the size and timing of foreign financial aid.

5.4 Labour resources and labour market

According to United Nations Office of the High Commissioner for Refugees (UNHCR) estimates, as of 6 June 2023, there were 6.28 million Ukrainian refugees outside the country, of which 5,935,300 were in Europe and 344,700 in non-European countries[20]. This considerable outflow is reflected in the population statistics (Table 2), according to which the population of Ukraine decreased from 41.0 million in 2021 to 34.8 million in 2022, and is expected to decrease further to 32 million by the end of 2023.

In addition, in January 2023, there were 5.5 million internally displaced people (IDPs) reported by the International Organisation for Migration (IOM, 2023). The number of refugees and IDPs was even larger at the beginning of the Russian aggression.

In July 2022, about 1 million people, primarily young men, were mobilised to the Ukrainian Armed Forces and other military, paramilitary, civil defence and security formations[21]. Probably, this number has not changed in a significant way.

All the above numbers significantly impact the labour-market situation, which is characterised by large-scale mismatches between demand for labour and its availability. On one hand, the unemployment rate increased from 9.8 percent in 2021 to 24.5 percent in 2022. On the other hand, the number of job vacancies is also high (IMF, 2023a).

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[19] For a preliminary assessment, see Centre for Economic Strategy, 'Economic Consequences of the Dam Destruction at the Kakhovka HPP', press release, 8 June 2023, https://ces.org.ua/en/economic-consequences-kakhovkahps-destruction/.
[20] See https://data.unhcr.org/en/situations/ukraine.
[21] Anna Kholodnova, 'The Minister of Defense named the number of Ukrainians mobilised to the Armed Forces', *Babel*, 8 July 2022, https://babel.ua/en/news/81183-the-minister-of-defense-named-the-number-of-ukrainians-mobilized-to-the-armed-forces.

5.5 Trade

In 2022, Ukraine's main export items were food (57.2 percent), metals (14.4 percent) and minerals (10.0 percent). The country's primary imports were machinery (26.4 percent), energy (22.6 percent), chemicals (16.8 percent) and food (10.6 percent). (see Tables 4-5). Between 2017 and 2022, the share of food products in Ukrainian exports increased, while the share of metals, in the past the dominant export item, decreased. The latter resulted, among others, from losing control over the South East territories and from war damage.

Table 4: Ukraine: exports of goods, by a group of products, % of the total, 2017-2022

Item	2017	2018	2019	2020	2021	2022
Foods	44.7%	42.9%	48.0%	49.1%	43.9%	57.2%
Mineral products	8.9%	9.0%	9.6%	11.0%	12.5%	10.0%
Chemicals	5.2%	5.5%	4.7%	5.1%	5.0%	4.1%
Woods	4.1%	4.5%	3.9%	3.9%	3.9%	5.2%
Industrial products	1.4%	1.5%	1.5%	1.6%	1.5%	1.4%
Metals	24.9%	26.3%	21.7%	19.5%	24.9%	14.4%
Machinery	7.2%	6.9%	7.4%	7.5%	6.1%	5.6%
Others	3.6%	3.4%	3.2%	2.3%	2.2%	2.2%

Source: National Bank of Ukraine.

Table 5: Imports of goods by a group of products, % of the total, 2017-2022

Item	2017	2018	2019	2020	2021	2022
Foods	8.6%	9.0%	9.4%	12.5%	11.0%	10.6%
Energy imports	24.3%	24.2%	20.9%	15.2%	20.1%	22.6%
Chemicals	19.4%	18.6%	18.0%	20.5%	20.6%	16.8%
Woods	2.3%	2.4%	2.1%	2.6%	2.1%	1.6%
Industrial products	4.3%	4.6%	5.1%	5.8%	5.3%	5.9%
Metals	5.8%	6.1%	5.8%	5.8%	6.1%	4.4%
Machinery	27.5%	28.5%	32.1%	33.5%	31.3%	26.4%
Others	7.8%	6.6%	6.5%	4.1%	3.6%	11.7%

Source: National Bank of Ukraine.

In 2022, exports of Ukrainian agricultural products (wheat, barley, maize, sunflower seeds and oil) met with serious logistical obstacles because of loss of access to the Azov Sea and some Black Sea ports, and the Russian blockade of Odesa. The Black Sea Grain Initiative, signed on 22 July 2022 by Russia and Ukraine under the auspices of the United Nations, and the government of Turkey, allowed unblocking partly these exports by establishing shipping corridors from the seaports Pivdennyi, Odesa and Chernomorsk[22]. The initiative was extended several times in the following months. However, the implementation of this deal experienced various obstacles from the Russian side, and its future remains uncertain. It did not allow grain shipments to return to the pre-war export capacity.

In April and May 2023, Ukrainian grain exports received another blow from the so-called frontline EU member states. In mid-April, Poland, Hungary, Slovakia and Bulgaria introduced unilateral bans on

[22] See BBC, 'What is the Ukraine grain deal?' 19 May 2023, https://www.bbc.com/news/world-61759692, and https://www.un.org/en/black-sea-grain-initiative/updates.

imports of Ukrainian grain (against the EU external trade policy rules). The EU introduced preventive safeguard measures, adopted by the European Commission on 2 May 2023 (Kleimann, 2023).

Since 2013, the EU has become Ukraine's leading trading partner (Zachmann *et al*, 2020), accounting for 60.7 percent of commodity exports and 44.4 percent of imports in 2022 (Tables 6-7). The war accelerated Ukraine's trade reorientation from countries of the former Soviet Union (mainly Russia) towards the EU. China became another 'victim' of the war: its share in Ukrainian exports halved in 2022 compared to 2021.

Table 6: Geographic structure of exports of goods, % of the total, 2017-2022

Destination	2017	2018	2019	2020	2021	2022
EU	34.4%	36.4%	35.9%	32.4%	36.2%	60.7%
former Soviet Union	17.5%	16.1%	14.4%	12.4%	10.7%	5.6%
China	5.1%	5.1%	7.6%	15.5%	12.5%	6.0%
United States	2.1%	2.5%	2.1%	2.1%	2.5%	2.1%
Africa	10.1%	9.3%	10.8%	8.9%	8.9%	5.2%
Others	30.7%	30.5%	29.2%	28.6%	29.2%	20.5%

Source: National Bank of Ukraine.

Table 7: Geographic structure of imports, % of the total, 2017-2022

Origin	2017	2018	2019	2020	2021	2022
EU	35.6%	35.2%	36.5%	40.3%	37.5%	44.4%
former Soviet Union	25.5%	25.2%	21.2%	16.7%	19.3%	8.0%
China	10.9%	13.0%	14.8%	15.4%	15.0%	14.7%
United States	4.9%	5.1%	5.2%	5.7%	4.6%	3.7%
Africa	1.2%	1.0%	1.0%	1.1%	1.2%	0.8%
Others	21.8%	20.5%	21.3%	20.8%	22.3%	28.4%

Source: National Bank of Ukraine.

5.6 Energy sector

Ukraine's energy sector was under permanent Russian attacks from the beginning of the war. Russian troops took control of two nuclear plans, Zaporizhska and Chornobylska. By March 2022, Russians had left Chornobylska nuclear plant, but Zaporizhska – the largest nuclear power plant in Europe – remained occupied and ceased production.

In October 2022, the Russian army unleashed regular massive missile attacks against energy infrastructure, aiming to create a humanitarian catastrophe for the civilian population, undermine the functioning of the Ukrainian state and economy, and weaken Ukraine's air defence at the frontlines. Between October 2022 and February 2023, 255 airstrikes (Topalov, 2023) against Ukrainian energy infrastructure caused several blackouts of the energy system. Since February 2023, the intensity of missile strikes against energy infrastructure has declined.

Due to occupied power plants and destroyed substations, Ukraine's electricity system remains precarious. Before the war, Ukraine had 47 gigawatts of generation capacity (up to about 22 GW was effectively used). According to the largest Ukrainian electricity company DTEK, the available capacities are now less than 10 GW.

Before the war, Ukraine started to prepare for integration into the continental European electricity system – coordinated by the European Network of Transmission System Operators for Electricity (ENTSO-E). After the invasion began, the Ukrainian energy system was disconnected from the Russian system (the legacy of the Soviet electricity network) and was synchronised with the continental European system. In June 2022, Ukraine began commercial electricity exports to the EU. However, missile strikes from October 2022 stopped these exports. At time of writing, the connection is used for exports and imports and serves as an essential infrastructure for stabilising the Ukrainian system.

Official data on energy production, supply and consumption in 2022 are unavailable in mid-June 2023, but expert estimates suggest that electricity consumption dropped by 31.5 percent y/y in 2022. Industrial consumption declined by 45 percent (in the steel industry by 52 percent), and household consumption declined by 16 percent compared to 2021[23].

Transit of Russian oil (the Druzhba [Friendship] pipeline system) and gas (Ukrainian gas transit system) through Ukrainian territory continues and is being paid for. However, volumes were low before the war and remain so now. It generates little revenue for the Ukrainian transit providers and Russian exporters.

At the same time, Ukraine managed the winter of 2022/2023 without direct imports of Russian natural gas. Thanks to the improved connectivity within the EU, Ukraine can meet its net-import demand, even if the Russian gas transit to Europe stops completely.

5.7 Transportation

Transportation has been performing exceptionally well from the start of the war. The state railway company Ukrzaliznytsya played a crucial role in evacuating people from the area of military action and bringing military supplies from the West. Ukrzaliznytsya also became the most vital instrument in exporting Ukrainian grain to foreign markets during the seaport blockade, which was in force until July 2022 (see subsection 5.5).

5.8 Agriculture

In 2022, agriculture output in constant 2016 prices decreased by 25 percent compared to 2021, according to the State Statistics Service of Ukraine[24]. Territorial losses can explain part of this decline, as the 2022 data covers only the territory under the control of the Ukrainian government. Crop production decreased by 28 percent, while animal production fell by 12 percent. Large agricultural enterprises lost more than family farms.

The planted area of cereals decreased by 23.9 percent y/y and the harvested area by 26.2 percent y/y. The physical volume of wheat production decreased by 35.5 percent y/y, maize by 37.8 percent y/y, barley by 40.6 percent y/y, sunflower seeds by 30.9 percent, and soya beans by 1.4 percent[25].

The decline was much more significant than expected. It was caused not only by direct military actions and war damages but also by increasing difficulties with pre-financing for purchasing fertilisers, seeds and other inputs, and finding a workforce in the war conditions.

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[23] Vadim Kolisnichenko, 'Ukrainian steelmakers reduced electricity consumption by 52% y/y in 2022', *GMK Center News*, 2 March 2023, https://gmk.center/en/news/ukrainian-steelmakers-reduced-electricity-consumption-by-52-y-y-in-2022/.

[24] See https://ukrstat.gov.ua/operativ/operativ2022/sg/psg_pc/pcg_pc_22_ue.xlsx.

[25] See https://ukrstat.gov.ua/operativ/operativ2023/sg/pvzu/pvzu_2022.xlsx.zip.

Most forecasts of agriculture production in 2023 remain pessimistic, amid sharp contraction of sown areas and reduced crop yields due to lower fertiliser investments.

5.9 Financial sector

The Ukrainian banking sector showed resilience during the initial stages of the Russian invasion, thanks to the NBU preventive measures. The NBU introduced targeted restrictions, allowing Ukrainian physical and legal persons to conduct banking transactions while preventing bank runs.

However, the Ukrainian banking system, especially state-owned banks, faced the problem of a high level of non-performing loans (NPLs) already before the war started. NPLs amounted to 30 percent in 2021 and 38 percent in 2022 (IMF, 2023a, p.15). Given many borrowers' war-related damages and losses, the NPL level will likely increase further in 2023.

The credit portfolio of banks has stalled, with state banks providing subsidised loans to the agriculture sector and micro-businesses. In 2022, the total credit portfolio remained at UAH 1.1 trillion ($34.1 billion), falling slightly to UAH 1.0 trillion ($31.1 billion) by the end of the year. Despite the war, deposits increased throughout 2022 amid abundant liquidity in the market. Over the first three months of the war, there was an outflow of deposits in foreign currency, but in the summer of 2022, the situation stabilised. In February 2023, the stock of hryvnia deposits was 32.2 percent higher than a year previously.

6 The EU accession process

During its meeting on 23-24 June 2022, the European Council (2022) granted Ukraine EU candidate status. However, to move to the next step in the EU accession process, ie opening EU accession negotiations, Ukraine must meet seven criteria set by the European Commission (2022). These are:

1. Enacting and implementing legislation on a selection procedure for judges of the Constitutional Court of Ukraine, including a pre-selection process based on evaluation of their integrity and professional skills, in line with Venice Commission recommendations;

2. Finalising the integrity vetting of the candidates for the High Council of Justice members by the Ethics Council and the selection of candidates to establish the High Qualification Commission of Judges of Ukraine;

3. Further strengthening the fight against corruption, in particular at a high level, through proactive and efficient investigations, and a credible track record of prosecutions and convictions; completing the appointment of a new head of the SACP Office by certifying the identified winner of the competition and launching and completing the selection process for a new Director of the NABU;

4. Ensuring that anti-money laundering legislation complies with the standards of the Financial Action Task Force; adopting a strategic plan for the reform of the entire law enforcement sector as part of Ukraine's security environment;

5. implementing the Anti-Oligarch law to limit the excessive influence of oligarchs in economic, political and public life; this should be done in a legally sound manner, taking into account the opinion of the Venice Commission on the relevant legislation;

6. Tackling the influence of vested interests by adopting a media law that aligns Ukraine with the EU audiovisual media services directive and empowers the independent media regulator;

7. Finalising the reform of the legal framework for national minorities as recommended by the Venice Commission and adopting immediate and effective implementation mechanisms.

The implementation of these recommendations is going slowly. In its fourth round of assessment (as of April 2023), the New Europe Center (2023) in Kyiv gave the Ukrainian authorities a score of 6.8 on a scale from 0 to 10, a slight improvement since the previous round in February 2023. The best score was for the implementation of recommendation No. 6 (score of 9), followed by recommendations No. 2, 3 and 7 (score of 8) and No. 4 (score of 6). The worst assessment applies to the reform of the Constitutional Court (score of 2) and the Anti-Oligarch Law, work on which has been effectively frozen because of the lack of an opinion from the Venice Commission.

The June 2023 assessment by the European Commissioner for Neighbourhood and Enlargement Oliver Varhelyi was even more nuanced[26]. According to him, Ukraine completed two steps: No. 2 (on two judicial bodies) and No. 6 (on media). It has also achieved *good* progress on step No. 1 (reform of the Constitutional Court). Concerning the remaining four steps, it has made *some* progress.

7 Conclusions and recommendations

The Russian aggression has already caused enormous human and material losses, turning back Ukraine in its socio-economic development by several decades. As the war continues and there are no prospects for its immediate end, the overall toll will further increase in the coming months.

Taken by surprise, the Ukrainian authorities had not only to organise effective military resistance against aggression but also adapt the country and economy's management to the realities of martial law. After the initial shock, the new management system was organised relatively quickly. It combined the unavoidable elements of command management (where necessary) with flexibility, allowing market adaptation and allocation mechanisms to work relatively smoothly and leaving sufficient room for local initiatives. Furthermore, this system was corrected with new challenges and circumstances and collected experience.

In the first months of the war, Ukraine had to rely mainly on its own military and economic resources. On the macroeconomic front, this caused severe tensions and challenges. The ballooning fiscal deficit had to be financed primarily by the NBU, causing inflationary pressures and creating the risk of a balance-of-payments crisis. Fortunately, since the second half of 2022, the flow of foreign financial aid has intensified and become more regular and predictable (similar to military assistance). It has allowed to gross international reserves to be increased, the FX market to be calmed, the exchange rate and budget to be stabilised, and some FX and banking restrictions to be relaxed. In parallel, a learning process of both government and economic agents has facilitated some normalisation in economic life, tax collection, resuming exports and imports, and quick fixing of damage to critical infrastructure, especially in the energy and transportation systems.

As long as the war continues, prolonging large-scale, regular and predictable financial aid to Ukraine will be critical for basic macroeconomic stability and sustainability and for delivery of essential public goods by the Ukrainian authorities. On the other hand, the Ukrainian authorities must refine and improve their war economic management, abstaining from administrative and command methods whenever possible, simplifying regulatory procedures, tax and customs administration, returning to competitive public procurement, and continuing market reforms and privatisation in cases that do not harm defence efforts. Particular attention should be given to the continuation of governance reforms,

[26] See 'Press remarks by Neighbourhood and Enlargement Commissioner Oliver Varhelyi, following the informal General Affairs Council', 22 June 2023, https://ec.europa.eu/commission/presscorner/detail/en/statement_23_3460.

especially of the judicial system and law-enforcement agencies, fighting corruption (and eliminating its systemic causes), limiting the influence of oligarchs, and other measures that can help start EU accession negotiations soon.

Once the war ends, Ukrainian authorities should stop applying the command methods of war management and launch a full-scale reform effort in all significant areas of economic and political governance (see Boyarchuk *et al*, 2023, for a comprehensive blueprint of economic and institutional reforms).

The international donor community must prepare itself not only to support a post-war reconstruction, but also to provide sufficient, stable and predictable current financial aid as long as the war continues and for some time after its end. The current financial aid and post-war reconstruction support should be accompanied by well-defined reform conditionality, that is realistic to implement in the war conditions.

The EU and its member states should lead in providing and coordinating financial aid. Such a role is justified by the EU's geographic proximity to Ukraine and the perspective of Ukraine's EU membership. It is in the EU's best interests to avoid macroeconomic destabilisation of Ukraine during the war, and to incentivise Ukrainian authorities to advance reforms as quickly as possible.

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